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Legislative Audit Division

State of Montana

Report to the Legislature

March 2005

Financial Audit

For the Fiscal Year Ended June 30, 2004

Montana Water Pollution Control and Drinking Water State Revolving Fund Programs

Department of Environmental Quality
Department of Natural Resources and Conservation

We performed a financial audit of the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs for the fiscal year ended June 30, 2004. This report contains the audited financial statements and accompanying notes for fiscal year 2003-04. We issued an unqualified opinion on the financial statements. This opinion means the reader may rely on the financial information presented.

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FINANCIAL AUDITS

Financial audits are conducted by the Legislative Audit Division to determine if the financial statements included in this report are presented fairly and the agency has complied with laws and regulations having a direct and material effect on the financial statements. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States Government Accountability Office. Financial audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) certificates.

Government Auditing Standards, the Single Audit Act Amendments of 1996 and OMB Circular A-133 require the auditor to issue certain financial, internal control, and compliance reports. This individual agency audit report is not intended to comply with these requirements and is therefore not intended for distribution to federal grantor agencies. The Legislative Audit Division issues a statewide biennial Single Audit Report which complies with the above reporting requirements. The Single Audit Report for the two fiscal years ended June 30, 2005, will be issued by March 31, 2006. The Single Audit Report for the two fiscal years ended June 30, 2003, was issued on March 23, 2004. Copies of the Single Audit Report can be obtained by contacting:

Single Audit Coordinator
Office of Budget and Program Planning
State Capitol
Helena MT 59620
Phone (406) 444-3616

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Deputy Legislative Auditors:
Jim Pellegrini, Performance Audit
Tori Hunthausen, IS Audit & Operations
James Gillett, Financial-Compliance Audit

March 2005

The Legislative Audit Committee
of the Montana State Legislature:

This is our report on the fiscal year 2003-04 financial audit of the Montana Water Pollution Control State Revolving Fund (WPCSRF) and Drinking Water State Revolving Fund (DWSRF) Programs. The Department of Natural Resources and Conservation requested the audit of these programs because annual audits are required by the federal Environmental Protection Agency.

The objectives of a financial audit include determining if the programs' financial statements present fairly their financial position at June 30, 2004, and the results of the programs' operations for the fiscal year then ended. We tested compliance with state and federal laws that have a direct and material impact on the financial statements.

The WPCSRF program provides loans at a reduced interest rate to finance construction of publicly-owned water pollution control facilities, nonpoint source pollution control projects, and estuary management plans. Water pollution control loans are comprised of federal grants and state match funds, and must be repaid within 20 years. As of June 30, 2004, the Water Pollution Control Program had $119,842,427 of outstanding loans, including advances from other funds.

The DWSRF program provides low interest loans to communities for the construction of drinking water treatment facilities. Drinking water loans are comprised of federal grants and state match funds, and may be financed up to 30 years. At June 30, 2004, the Drinking Water Program had $49,305,146 of outstanding loans.

On page A-1, you will find the Independent Auditor's Report followed by the financial statements and accompanying notes. We issued an unqualified opinion which means the reader can rely on the presented information. The programs' financial statements begin on page A-3. Our opinion on the programs' supplementary financial information is on page B-1. The supplementary information begins on page B-3. Beginning on page C-1 is our report on compliance and internal control which is required by Government Auditing Standards issued by the Comptroller General of the United States.

Officials from both departments have reviewed this report and agree with the contents. We thank the directors of the Department of Environmental Quality and the Department of Natural Resources and Conservation and their staff for cooperation and assistance during the audit.

Respectfully submitted,

Scott A. Seacat
Legislative Auditor

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Department of Environmental Quality	Richard Opper, Director Tom Livers, Deputy Director Dean Rude, Chief Financial Officer, Financial Services
Department of Natural Resources and Conservation	Mary Sexton, Director Anna Miller, Financial Advisor Ann Bauchman, Administrator, Centralized Services Division

For additional information concerning the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs, contact Anna Miller, Financial Advisor, at:

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The audit staff involved in this audit were Jim Manning, Alexa O'Dell, and Jeff Tamblyn.

LEGISLATIVE AUDIT DIVISION

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John W. Northey, Legal Counsel

Deputy Legislative Auditors:
Jim Pellegrini, Performance Audit
Tori Hunthausen, IS Audit & Operations
James Gillett, Financial-Compliance Audit

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying Combined Balance Sheet of the Montana Water Pollution Control State Revolving Fund and Drinking Water State Revolving Fund as of June 30, 2004, and the related Combined Statement of Revenues, Expenditures, and Changes in Fund Balance for the fiscal year then ended. The information contained in these financial statements is the responsibility of the management of the Montana Department of Environmental Quality and the Montana Department of Natural Resources and Conservation (departments). Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in the notes to the financial statements, the financial statements of the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs are intended to present the financial position and results of operations of only that portion of the financial reporting entity of the state of Montana that is attributable to the transactions of the programs.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs as of June 30, 2004, and results of operations for the fiscal year then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated January 24, 2005, on our consideration of the departments' compliance with laws and regulations and the departments' internal control structures.

Respectfully submitted,

James Gillett, CPA
Deputy Legislative Auditor

January 24, 2005

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MONTANA WATER POLLUTION CONTROL AND DRINKING WATER
STATE REVOLVING FUND PROGRAMS
COMBINED BALANCE SHEET
SPECIAL REVENUE AND DEBT SERVICE FUNDS
JUNE 30, 2004

	WATER POLLUTION CONTROL			DRINKING WATER			
	STATE SPECIAL REVENUE	FEDERAL SPECIAL REVENUE	DEBT SERVICE	STATE SPECIAL REVENUE	FEDERAL SPECIAL REVENUE	DEBT SERVICE	TOTAL
ASSETS							
Cash and Cash Equivalents	$8,159,184	($41,852)	$645,518	$4,035,072	$50,989	$443,653	$13,292,564
Interest Receivable	345,293		1,486,166	152,202		626,723	2,610,384
Due from Federal Government		19,402			168,855		188,257
Investments	7,372,459		1,648,972	5,331,850	1	1,077,784	15,431,066
Loans Receivable	108,484,204			49,305,146			157,789,350
Advances from Other Funds	11,358,223						11,358,223
Total Assets	$135,719,363	($22,450)	$3,780,656	$58,824,270	$219,845	$2,148,160	$200,669,844
LIABILITIES AND FUND BALANCES							
Liabilities:							
Accounts Payable	$11,572	$650	$1,217	$503	$106,290		$120,232
Payroll Payable	2,716	11,587		5,718	30,821		50,842
Deferred Revenue		59			19,382		19,441
Inter-entity Loans Payable	20,954	5,000		691	1,781		28,426
Total Liabilities	$35,242	$17,296	$1,217	$6,912	$158,274		$218,941
Fund Balances							
Reserved for Loans Receivable	$119,842,427			$49,305,146			$169,147,573
Unreserved, Undesignated	15,841,694	(39,746)	3,779,439	9,512,212	61,571	2,148,160	$31,303,330
Total Fund Balances	$135,684,121	($39,746)	$3,779,439	$58,817,358	$61,571	$2,148,160	$200,450,903
Total Liabilities and Fund Balances	$135,719,363	($22,451)	$3,780,656	$58,824,270	$219,845	$2,148,160	$200,669,844

The accompanying notes to the financial statements are an integral part of this statement.

MONTANA WATER POLLUTION CONTROL AND DRINKING WATER
STATE REVOLVING FUND PROGRAMS
COMBINED STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE
SPECIAL REVENUE AND DEBT SERVICE FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

	WATER POLLUTION CONTROL			DRINKING WATER			
	STATE SPECIAL REVENUE	FEDERAL SPECIAL REVENUE	DEBT SERVICE	STATE SPECIAL REVENUE	FEDERAL SPECIAL REVENUE	DEBT SERVICE	TOTAL
REVENUES:							
Federal Capitalization Grant Revenue		$17,753,403			$5,872,705		$23,626,108
Interest Income on Investments	51,422		(97,953)	(249,561)		166,016	(130,076)
Interest Earnings from Loans	860,433		3,375,419	383,184		1,518,210	6,137,246
Administration and Origination Fees	445,087			35,976			481,063
Other Income	28	34			112		174
TOTAL REVENUES	$1,356,970	$17,753,437	$3,277,466	$169,599	$5,872,817	$1,684,226	$30,114,515
EXPENDITURES:							
Program Administration/Set-Asides	$72,457	$338,636		$31,004	$1,147,392		$1,589,489
TOTAL EXPENDITURES	$72,457	$338,636		$31,004	$1,147,392		$1,589,489
Excess Revenues Over (Under) Expenditures	$1,284,513	$17,414,801	$3,277,466	$138,595	$4,725,425	$1,884,226	$28,525,026
OTHER FINANCING SOURCES:							
General Obligation Bonds Proceeds	2,665,000						$2,665,000
General Obligation Bond Premium			878				878
Operating Transfers In:							
Recycled Transfer from Drinking Water WRF	2,559,810						2,559,810
Recycled Transfer from Water Pollution Control SRF				42,893			42,893
Debt Service Sweep	566,962			432,862			999,824
Transfer Bond Anticipation Note to Debt Service	2,000,000						2,000,000
Transfer Bond and BAN Proceeds to Debt Service			1,600,000				1,600,000
Loan Origination/Administrative Fees Transfer			282,250			22,842	305,092
Loan Loss Reserve Sweep	801,835			331,226			1,133,061
Federal Capitalization Grants	17,462,823			4,685,582			22,148,205
Total Other Financing Sources	$26,058,230		$1,883,128	$5,492,563		$22,842	$33,454,763
OTHER FINANCING USES:							
Bond Principal			$550,000			$335,000	$885,000
Bond Interest			697,966			427,487	1,125,453
Bonds Cost of Issuance	71,471			(6,330)			65,141
Operating Transfers Out:							
Recycled Transfer to Water Pollution Control SRF				2,559,810			2,559,810
Recycled Transfer to Drinking Water WRF	42,893						42,893
Debt Service Sweep			566,962			432,862	999,824
Transfer Bond Anticipation Note to Debt Service			2,000,000				2,000,000
Transfer Bond and BAN Proceeds to Debt Service	1,600,000						1,600,000
Loan Origination/Administrative Fees Transfer	282,250			22,842			305,092
Loan Loss Reserve Sweep			801,835	0		331,226	1,133,061
Federal Capitalization Grants		17,462,623			4,685,582		22,148,205
Total Other Financing Uses	$1,896,614	$17,462,623	$4,616,783	$2,576,322	$4,685,582	$1,526,575	$32,864,479
Excess (deficiency) of revenues and other financing sources over (under) expenditures and other financing uses	$25,344,129	($47,822)	$543,831	$3,054,836	$39,843	$180,493	$29,115,310
Fund Balance July 1, 2003	$110,321,207	$0	$3,236,486	$55,788,501	($30,260)	$1,967,667	$171,283,601
Prior Year and Federal Revenue Adjustments	18,785	8,076	(878)	(25,979)	51,988	0	51,992
Fund Balance June 30, 2004	$135,684,121	($39,746)	$3,779,439	$58,817,358	$61,571	$2,148,160	$200,450,903

The accompanying notes to the financial statements are an integral part of this statement.

MONTANA STATE WATER POLLUTION CONTROL AND DRINKING WATER STATE REVOLVING FUND PROGRAMS
SPECIAL REVENUE AND DEBT SERVICE FUND
NOTES TO FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

1. Organization of the Programs

The State of Montana's Water Pollution Control State Revolving Fund (WPCSRF) Program was established pursuant to Title VI of the Federal Water Quality Act of 1987. This federal act established the WPCSRF program to replace the construction grants program to provide a flexible financing source to loan money at reduced interest rates to finance the construction of publicly owned water pollution control facilities, non-point source pollution control projects, and estuary management plans. Instead of making grants to communities that pay for a portion of building wastewater treatment facilities, the WPCSRF provides for low interest rate loans to finance the entire cost of qualified projects.

The State of Montana's Drinking Water State Revolving Fund (DWSRF) Program was established pursuant to Title XIV of the Safe Drinking Water Act. This federal act established the DWSRF program for states to make loans to community water systems and non-profit non-community water systems. Instead of making grants to communities that pay for a portion of building drinking water treatment facilities, the DWSRF provides for low interest rate loans to finance the entire cost of qualified projects or to refinance debt obligations on projects that began after July 1, 1993. The State of Montana first incurred expenditures in the DWSRF Program in state fiscal year (SFY) 1997.

WPCSRF loans must be repaid within 20 years while DWSRF loan agreements allow up to 30 years for repayment. All repayments of interest and principal must remain in the revolving funds. Both programs are capitalized through U.S. Environmental Protection Agency (EPA) grants. States are required to provide 20 percent of the federal capitalization grant as matching funds in order to receive a grant. The State of Montana issues General Obligation Bonds to provide the required state matching funds.

The programs are administered jointly by the Department of Environmental Quality (DEQ) Technical and Financial Assistance Bureau, and the Conservation and Resource Development Division of the Department of Natural Resources and Conservation (DNRC). The revolving fund programs do not have any full time employees. Both funds are charged for time spent on SRF activities by department employees. The charges include salaries and benefits of the employees and operating expenses as well as indirect costs.

2. Summary of Significant Accounting Policies

A. State Revolving Fund (SRF) Program Fund Structure

Both programs use Special Revenue and Debt Service funds, as appropriate, to report the financial position and the results of operations. A Special Revenue Fund accounts for the proceeds of specific revenue sources that are restricted to expenditures for specified purposes (other than expendable trusts or major capital projects). A Debt Service Fund accounts for

resources accumulated for payment of principal and interest on general long-term obligation debt. Montana maintains a State Special Revenue and a Federal Special Revenue Fund. The SRF program revenue and expenses include transactions from each Special Revenue Fund. Special Revenue and Debt Service Funds are considered governmental funds.

A fund is a separate accounting entity with a self-balancing set of accounts. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions and activities.

B. Basis of Accounting

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. All governmental funds are accounted for using a current financial resources measurement focus. With this measurement focus, only assets and current liabilities generally are included on the balance sheet. Operating statements of governmental funds present increases (revenues and other financing sources) and decreases (expenditures and other financing uses) in net current assets.

Governmental funds use the modified accrual basis of accounting. The modified accrual basis is the accrual basis adapted to the governmental fund-type measurement focus. Under the modified accrual basis of accounting, revenues are recorded when received in cash unless susceptible to accrual. Revenues are susceptible to accrual if they are measurable and available within sixty days after the end of the fiscal year to finance expenditures of the fiscal year. Revenues are deferred if material and received before the normal time of receipt or if received for a particular activity and the expense for that activity has not been incurred prior to fiscal year-end. Expenditures are recognized when the related fund liability is incurred, with the following exceptions:

1) principal and interest on long-term debt are recognized when due;
2) prepayments are accounted for as expenditures in the period of acquisition;
3) inventory items are considered expenditures when purchased.

The Loans Receivable account resides in the State Special Revenue fund for each program. This account represents the total principal due on the loans outstanding for each program.

3. Cash/Cash Equivalents

Cash and cash equivalents consist of funds deposited with the US Bank, N.A. as trustee, and investments categorized as cash equivalents, which are short-term, highly liquid investments with original maturities of three months or less.

Risk Category 1	Carrying Amount	Fair Value	Fund
Money Market Direct Investment	$9,921,475	$9,921,475	Various

4. Investments

The Board of Examiners of the State of Montana authorizes the sale of general obligation bonds to provide the state match for the SRF programs through the issuance of an Indenture of Trust. The Board of Examiners is comprised of the Governor, Attorney General and the Secretary of State for the State of Montana. The Indenture of Trust specifies the eligible investments meeting defined rating and risk criteria in which the state may invest. The state invests funds through its trustee bank, US Bank, N.A.

Security Type	Category 1	Carrying Amount	Market Value
Government Securities	$18,430,008	$18,430,008	$18,238,038

5. Loans Receivable

Montana operates both SRF programs as direct loan programs. Loans made to communities through the Water Pollution Control Program are funded 83.33 percent by the federal EPA capitalization grant, and 16.67 percent by the state match amount. Loans also are made as recycled, or "second round", loans and are disbursed from loan repayment funds. Loans made by the Drinking Water Program are funded approximately 80 percent by the federal EPA capitalization grant, and 20 percent by the state match amount. Loan funds are disbursed to the local borrower agencies by the trustee bank as the local borrower agencies expend funds for the purposes of the loan and request reimbursement from the program. Interest is calculated from the date that funds are disbursed. Typically after the final disbursement has been made, the payment schedule is certified in the loan agreement and adjusted for the actual amounts disbursed. No provision for uncollectible accounts has been made as all loans are current in terms of compliance with the repayment schedules, and management believes that all loans will be repaid according to the terms of the loan agreement.

The drawn and outstanding principal balance of all loans guaranteed by the WPCSRF Program as of June 30, 2004 is $119,842,427. The total loans receivable in the WPCSRF program includes $11,358,223 classified as advances from other funds. The advances are inter-fund loans within the Department of Natural Resources and Conservation used for the non-point source private loans program. The drawn and outstanding principal balance of all loans guaranteed by the DWSRF Program as of June 30, 2004 is $49,305,146.

Loans mature at various intervals through July 1, 2031. The scheduled principal payments on loans and advances from other funds maturing in the years following state fiscal year (SFY) 2004 are as follows:

SFY ending June 30:	WPCSRF Amount	DWSRF Amount
2005	$ 6,382,432	$ 1,845,410
2006	$ 6,427,300	$ 2,202,370
2007	$ 6,671,000	$ 2,408,410
2008	$ 6,926,000	$ 2,402,970
2009 and thereafter	$ 93,435,695	$ 40,445,986
Total	**$ 119,842,427**	**$ 49,305,146**

As of June 30, 2004, the WPCSRF and DWSRF had authorized loans to public entities of the State of Montana that in the aggregate exceeded $172 and $58 million, respectively. The outstanding balances of the largest loans in each portfolio are as follows:

Water Pollution Control State Revolving Fund:

Local Agency	Authorized Loan Amount	Outstanding Balance
City of Great Falls	$ 12,100,000	$ 10,426,046
City of Helena	$ 9,320,000	$ 8,929,000
Big Sky County Water & Sewer	$ 7,000,000	$ 6,326,076
Big Sky County Water & Sewer	$ 6,500,000	$ 3,867,169
Big Sky County Water & Sewer	$ 5,513,000	$ 3,474,000
City of Lewistown	$ 5,400,000	$ 0
Missoula WWTP	$ 5,000,000	$ 4,747,000
Missoula County Mullan Rd RSID 8474	$ 4,729,000	$ 3,736,043
City of Missoula SID 524	$ 4,577,000	$ 4,243,228
City of Great Falls	$ 4,400,000	$ 1,296,012
Total	**$ 64,539,000**	**$ 47,044,574**

Drinking Water State Revolving Fund:

Local Agency	Authorized Loan Amount	Outstanding Balance
City of Havre II	$ 8,401,000	$ 8,216,000
City of Whitefish II	$ 5,839,000	$ 5,007,000
City of Laurel	$ 5,250,000	$ 4,192,000
City of East Helena II	$ 3,234,000	$ 2,943,000
City of Great Falls	$ 3,000,000	$ 2,629,921
Laurel II	$ 2,541,000	$ 2,428,888
River Rock Water & Sewer	$ 2,100,000	$ 2,050,000
Big Sky County Water & Sewer	$ 1,966,000	$ 1,878,366
City of Conrad II	$ 1,543,172	$ 1,412,000
Fort Peck Rural County WD	$ 1,520,000	$ 1,361,410
Total	**$ 35,394,172**	**$ 32,118,585**

6. Interest Receivable

The interest receivable represents interest owed by borrowers as of June 30, 2004, for the July 1, 2004 payment. It represents the six months of interest accrued from the previous loan payments due January 1, 2004. It does not include interest payments received in June that were due July 1, 2004. Interest payments received during June 2004 amounted to $305,123 for the WPCSRF and $177,833 for the DWSRF.

7. Bonds Payable

Water Pollution Control SRF general obligation bonds payable at June 30, 2004 were as follows:

Series 1994B

Payable during the year ending June 30,	Interest Range (%)	Principal	Interest	Total
2005	4.20 - 6.10	$ 95,000	$ 90,268	$ 185,268
2006		100,000	85,050	185,050
2007		105,000	79,463	184,463
2008		110,000	73,495	183,495
2009		120,000	66,995	186,995
2010-2014		710,000	218,208	928,208
2015-2016		350,000	21,655	371,655
Total Cash Requirements		$1,590,000	$ 635,134	$ 2,225,134

Series 1996C

Payable during the year ending June 30,	Interest Range (%)	Principal	Interest	Total
2005	3.75 – 5.75	$ 135,000	$ 108,565	$ 243,565
2006		140,000	101,620	241,620
2007		145,000	94,280	239,280
2008		155,000	86,403	241,403
2009		160,000	77,975	237,975
2010-2014		960,000	241,134	1,201,134
2015-2017		345,000	30,331	375,331
Total Cash Requirements		$2,040,000	$ 740,308	$ 2,780,308

Series 1998A

Payable during the year ending June 30,	Interest Range (%)	Principal	Interest	Total
2005	3.75 – 5.15	$ 140,000	$ 135,727	$ 275,727
2006		145,000	129,635	274,635
2007		150,000	123,218	273,218
2008		155,000	116,469	271,469
2009		165,000	109,308	274,308
2010-2014		940,000	420,972	1,360,972
2015-2019		1,190,000	157,898	1,347,898
Total Cash Requirements		$2,885,000	$ 1,193,227	$ 4,078,227

Series 2000B

Payable during the year ending June 30,	Interest Range (%)	Principal	Interest	Total
2005	4.25 – 5.60	$ 115,000	$ 155,181	$ 270,181
2006		120,000	149,570	269,570
2007		125,000	143,659	268,659
2008		130,000	137,459	267,459
2009		135,000	130,983	265,983
2010-2014		810,000	540,740	1,350,740
2015-2019		1,065,000	296,684	1,361,684
2020-2021		520,000	29,618	549,618
Total Cash Requirements		$3,020,000	$ 1,583,894	$ 4,603,894

Series 2001H

Payable during the year ending June 30,	Interest Range (%)	Principal	Interest	Total
2005	4.00 – 5.00	$ 100,000	$ 111,196	$ 211,196
2006		100,000	107,196	207,196
2007		105,000	103,096	208,096
2008		110,000	98,796	208,796
2009		115,000	94,296	209,296
2010-2014		630,000	397,330	1,027,330
2015-2019		785,000	238,366	1,023,366
2020-2022		570,000	43,638	613,638
Total Cash Requirements		$2,515,000	$ 1,193,914	$ 3,708,914

Series 2003D

Payable during the year ending June 30,	Interest Range (%)	Principal	Interest	Total
2005	2.00 – 3.75	$ 145,000	$ 79,150	$ 224,150
2006		155,000	76,150	231,150
2007		160,000	73,000	233,000
2008		160,000	69,800	229,800
2009		165,000	66,426	231,426
2010-2014		900,000	264,046	1,164,046
2015-2019		1,045,000	100,784	1,145,784
Total Cash Requirements		$2,730,000	$ 729,356	$ 3,459,356

Series 2004A

Payable during the year ending June 30,	Interest Range (%)	Principal	Interest	Total
2005	2.00 – 4.50	$ 0	$ 66,462	$ 66,462
2006		125,000	92,948	217,948
2007		150,000	90,198	240,198
2008		150,000	87,198	237,198
2009		155,000	83,760	238,760
2010-2014		845,000	346,154	1,191,154
2015-2019		1,010,000	168,554	1,178,554
2020		230,000	5,175	235,175
Total Cash Requirements		$2,665,000	$ 940,449	$ 3,605,449

Total General Obligation Debt - WPCSRF

Payable during the year ending June 30,	Principal	Interest	Total
2005	$ 730,000	$ 746,549	$ 1,476,549
2006	885,000	742,169	1,627,169
2007	940,000	706,914	1,646,914
2008	970,000	669,620	1,639,620
2009	1,015,000	629,743	1,644,743
2010-2014	5,795,000	2,428,584	8,223,584
2015-2019	5,790,000	1,014,272	6,804,272
2020-2022	1,320,000	78,431	1,398,431
Total Cash Requirements	17,445,000	$ 7,016,282	$ 24,461,282

Drinking Water SRF general obligation bonds payable at June 30, 2004 were as follows:

Series 1998F

Payable during the year ending June 30,	Interest Range (%)	Principal	Interest	Total
2005	3.60 – 4.85	$ 130,000	$ 113,317	$ 243,317
2006		130,000	108,182	238,182
2007		140,000	102,747	242,747
2008		145,000	96,940	241,940
2009		150,000	90,855	240,855
2010-2014		845,000	349,600	1,194,600
2015-2019		1,055,000	130,731	1,185,731
Total Cash Requirements		$2,595,000	$ 992,372	$ 3,587,372

Series 2000A

Payable during the year ending June 30,	Interest Range (%)	Principal	Interest	Total
2005	4.25 – 5.60	$ 100,000	$ 139,075	$ 239,075
2006		105,000	134,180	239,180
2007		110,000	128,993	238,993
2008		120,000	123,401	243,401
2009		125,000	117,413	242,413
2010-2014		725,000	397,330	1,122,330
2015-2019		955,000	238,366	1,193,366
2020-2021		465,000	43,638	508,638
Total Cash Requirements		$2,705,000	$ 1,322,396	$ 4,027,396

Series 2001G

Payable during the year ending June 30,	Interest Range (%)	Principal	Interest	Total
2005	4.00 – 5.00	$ 115,000	$ 132,066	$ 247,066
2006		120,000	124,866	244,866
2007		125,000	122,466	247,466
2008		125,000	117,466	242,466
2009		135,000	112,266	247,266
2010-2014		755,000	472,273	1,227,273
2015-2019		935,000	283,301	1,218,301
2020-2022		675,000	51,491	726,491
Total Cash Requirements		$2,985,000	$ 1,416,195	$ 4,401,195

Series 2003E

Payable during the year ending June 30,	Interest Range (%)	Principal	Interest	Total
2005	2.00 – 3.75	$ 90,000	$ 48,636	$ 138,636
2006		95,000	46,786	141,786
2007		95,000	44,886	139,886
2008		100,000	42,936	142,936
2009		100,000	40,861	140,861
2010-2014		545,000	162,957	707,957
2015-2019		650,000	62,814	712,814
Total Cash Requirements		$1,675,000	$ 449,876	$ 2,124,876

Total General Obligation Debt - DWSRF

Payable during the year ending June 30,	Principal	Interest	Total
2005	$ 435,000	$ 433,094	$ 868,094
2006	450,000	414,014	864,014
2007	470,000	399,092	869,092
2008	490,000	380,743	870,743
2009	510,000	361,395	871,395
2010-2014	2,870,000	1,382,160	4,252,160
2015-2019	3,595,000	715,212	4,310,212
2020-2022	1,140,000	95,129	1,235,129
Total Cash Requirements	$ 9,960,000	$ 4,180,839	$ 14,140,839

8. Fund Balance

A portion of the fund balance in the WPCSRF and DWSRF has been reserved for Loans and Advances Receivable, indicating that a portion of the fund balance is not available for current expenditures.

9. Program Capitalization

The WPCSRF and DWSRF programs are capitalized by grants from the Environmental Protection Agency (EPA) and matching funds from the State of Montana. All grant funds drawn are recorded as revenue. As of June 30, 2004, the EPA has awarded capitalization grants of $108,917,065 to the State of Montana for the WPCSRF program; $162,945,133 has been drawn from federal and state funds for loans and administrative expenses. As of June 30, 2004, the EPA has awarded capitalization grants of $61,013,964 to the State of Montana for the DWSRF program; $60,410,669 has been drawn from federal and state funds for loans and administrative expenses. Montana has issued general obligation bonds totaling $22,480,000 for use as state matching funds for the WPCSRF program and $10,920,000 for use as state matching funds in the DWSRF program.

10. Federal Capitalization Grant Revenues

Actual draws of federal funds differ from the amount of Federal Capitalization Grant Revenue reported on the Statement of Revenues, Expenditures and Changes in Fund Balance. This occurs because state accounting policy requires federal special revenue funds reflect a zero fund balance at fiscal year-end (with the exception of "A" accruals). Consequently, if a positive fund balance exists, deferred revenue is recorded. If a negative fund balance is reflected at fiscal year-end, a revenue accrual to record revenue is recorded to zero the fund balance.

The following is a reconciliation of federal revenues reported on the financial statements to federal cash actually drawn during the state fiscal year:

WPCSRF

Federal Capital Grant Revenue – Combined Statement	$17,753,403
Adjustment Due from Federal Govt. FY03	25,335
Adjustment Deferred Revenue FY03	(43)
Adjustment Due from Federal Govt. FY04	(19,402)
Adjustment Deferred Revenue FY04	59
Other Adjustments	(16)
Total Federal Draws	**$17,759,336**

DWSRF

Federal Capital Grant Revenue – Combined Statement	$ 5,872,705
Adjustment Due From Federal Govt. FY03	248,115
Adjustment Deferred Revenue FY03	(30,395)
Adjustment Due from Federal Govt. FY04	(168,855)
Adjustment Deferred Revenue FY04	19,382
Other Adjustments	(76)
Total Federal Draws	**$ 5,940,876**

11. Interest Income on Investments

This revenue represents interest earnings on investments in the various accounts within the Funds. All assets of the Funds are fully invested, to the degree possible, in investment vehicles by the trustee. The investments range from cash equivalents to long-term investments.

12. Interest Earnings

This revenue represents interest earnings from loan repayments made by borrowers. A typical loan carries an interest rate of 4%; however, during fiscal year 2004 the rate was decreased to 3.75% for new loans. The 3.75% is comprised of a loan interest rate of 2.00%, as well as a 1.00% Loan Loss Reserve fee and a 0.75% Special Administration fee. The earnings for each of these components totaled $2,448,794, $983,038, and $804,020, respectively, for the Water Pollution Control SRF program, and $1,120,554, $408,127, and $372,712, respectively, for the Drinking Water SRF program. Disadvantaged communities can receive loans with an interest rate of 2.75% because no Loan Loss Reserve fee is levied.

13. Program Administration and Set-Aside Funds

This expenditure represents costs incurred by DEQ and DNRC to administer the SRF programs. This amount is limited to 4% of each grant award from the EPA. Program Administration appears under the Resource Development/Recreation function in the State of Montana Combined Annual Financial Report (CAFR).

The DWSRF program includes several "sub-programs", called set-asides, which states can elect. A State may use a certain portion of its capitalization grants for the following activities:

- up to 4 percent of its capitalization grants to administer the DWSRF and provide technical assistance to public water systems;
- up to 2 percent of its grants to provide assistance to small public water systems;
- up to 10 percent of its grants for state program management activities, including administration of the State Public Water System Supervision Program, administration of the source water protection program, development and implementation of the capacity development and operator certification programs;
- up to 15 percent of its grants to assist in the development and implementation of local drinking water protection initiatives and other State programs.

In the DWSRF, the 4 percent administrative set-aside must be deposited to a separate fund, and must have separate accounting and disclosure.

DWSRF Program Administration/Set-Asides Detail:

Administration	$ 402,153
Technical Assistance	126,967
Program Management	355,044
Local Assistance	96,054
Other Expenses	198,178
Total Administration and Set-Asides	$1,178,396

14. Other Financing Sources and Uses

The Recycled Transfer from the DWSRF to the WPCSRF represents the amount transferred between the two programs to fund water pollution control project loans. At the discretion of the Governor, the state may transfer up to 33 percent of the DWSRF capitalization grant to the WPCSRF or an equal amount from the WPCSRF to the DWSRF. The transferred funds are "recycled" such that they consist of principal repayments from previous loans for drinking water projects.

Loan interest amounts received that exceed the debt service requirements are shown as a Financing Source and Use on the financial statements. The balance remaining in the Debt Service fund is transferred to the Investment fund. Both funds are within the State Revolving Fund. This occurs after payments are made to the bondholders on July 15 of each year. In the Arbitrage Certificate, this activity is termed a Debt Service Sweep.

Administration and Origination Fees are shown as both a Financing Source and Use of funds because the fees are initially recorded inside the Loan Account when disbursed. These revenues are then transferred to the Special Administration and Loan Loss Reserve funds that are outside of the State Revolving Fund.

The Loan Loss Reserve Sweep represents cash in excess of the reserve requirement that is transferred from the Loan Loss Reserve fund to the Principal fund per the bond indenture. The Loan Loss Reserve fund is considered outside of the Revolving Fund

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
John W. Northey, Legal Counsel

Deputy Legislative Auditors:
Jim Pellegrini, Performance Audit
Tori Hunthausen, IS Audit & Operations
James Gillett, Financial-Compliance Audit

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

Our audit was conducted for the purpose of forming an opinion on the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs' financial statements taken as a whole. The Schedule of Revolving and Non-Revolving SRF Program Assets, Special Revenue and Debt Service Funds, for the Montana Water Pollution Control and Drinking Water Programs and the related Schedule of Revolving and Non-Revolving SRF Program Revenues, Expenditures, and Changes in Fund Balance, Special Revenue and Debt Service Funds are presented for purposes of additional analysis and are not a required part of the financial statements of these programs. Such information has been subjected to the auditing procedures applied in the audit of the programs' financial statements and, in our opinion, based upon our audit, is fairly presented in all material respects in relation to the programs' financial statements taken as a whole.

Respectfully submitted,

James Gillett, CPA
Deputy Legislative Auditor

January 24, 2005

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MONTANA WATER POLLUTION CONTROL AND DRINKING WATER
SCHEDULE OF REVOLVING AND NON-REVOLVING SRF PROGRAM ASSETS
SPECIAL REVENUE AND DEBT SERVICE FUNDS
REGULATORY BASIS [1]
JUNE 30, 2004

	WPC-SRF SPECIAL REVENUE		WPC-SRF DEBT SERVICE FUND		Drinking Water SPECIAL REVENUE		Drinking Water DEBT SERVICE FUND		
	REVOLVING FUND	NON REVOLVING FUND	REVOLVING FUND	NON REVOLVING FUND	REVOLVING FUND	NON REVOLVING FUND	REVOLVING FUND	NON REVOLVING FUND	TOTAL
ASSETS									
Cash and Cash Equivalents	$7,634,309	$483,023	$610,702	$34,815	$3,784,763	$301,298	$267,822	$175,831	13,292,564
Interest Receivable		345,293	1,030,450	455,716		152,202	455,694	171,029	2,610,384
Due From Federal Government	19,402				168,855				188,257
Investments	2,627,302	4,745,157	1,619	1,647,354	4,112,468	1,219,383	350,109	727,675	15,431,066
Loans Receivable	108,484,204				49,305,146				157,789,350
Advances from Other Funds	11,358,223								11,358,223
Total Assets	$130,123,440	$5,573,473	$1,642,771	$2,137,885	$57,371,232	$1,672,883	$1,073,625	$1,074,535	$200,669,844
LIABILITIES AND FUND BALANCES									
Liabilities:									
Accounts Payable	$780	$11,442	$1,217		$106,290	$503			$120,232
Payroll Payable	13,909	394			30,821	5,718			50,842
Deferred Revenue	59				19,382				19,441
Inter-entity Loans Payable	25,954				1,781	691			28,426
Total Liabilities	$40,702	$11,836	$1,217		$158,274	$6,912			$218,941
Fund Balances									
Reserved for Loans Receivable	$119,842,427				$49,305,146				169,147,573
Unreserved, Undesignated	10,240,311	5,561,637	1,641,554	2,137,885	7,907,812	1,665,971	1,073,625	1,074,535	31,303,330
Total Fund Balances	$130,082,738	$5,561,637	$1,641,554	$2,137,885	$57,212,958	$1,665,971	$1,073,625	$1,074,535	$200,450,903
Total Liabilities and Fund Balances	$130,123,440	$5,573,473	$1,642,771	$2,137,885	$57,371,232	$1,672,883	$1,073,625	$1,074,535	$200,669,844

This schedule is prepared on a regulatory basis of presentation, rather than a GAAP (1) basis, as requested by the Environmental Protection Agency (EPA) for the Water Pollution Control and Drinking Water State Revolving Fund (SRF) Programs. This presentation separates certain regulated Revolving Fund (within the Fund) and Non-Revolving Fund (outside the Fund) activity by fund type. All proceeds from the EPA Capitalization Grant, corresponding state matching funds, and loan principal and interest repayments must be deposited into the Revolving Fund under Title VI of the Clean Water Act and Title XIV of the Safe Drinking Water Act. Other proceeds, including

(1) Generally Accepted Accounting Principles (GAAP).

MONTANA WATER POLLUTION CONTROL AND DRINKING WATER
SCHEDULE OF REVOLVING AND NON-REVOLVING SRF PROGRAM
REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE
SPECIAL REVENUE AND DEBT SERVICE FUNDS
REGULATORY BASIS [1]
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

	WPC-SRF SPECIAL REVENUE		WPC-SRF DEBT SERVICE FUND		Drinking Water SPECIAL REVENUE		Drinking Water DEBT SERVICE FUND		
	REVOLVING FUND	NON REVOLVING FUND	REVOLVING FUND	NON REVOLVING FUND	REVOLVING FUND	NON REVOLVING FUND	REVOLVING FUND	NON REVOLVING FUND	TOTAL
REVENUES:									
Federal Capitalization Grant Revenue	$17,753,403				$5,872,705				$23,626,108
Interest Income on Investments	94,657	($43,235)	$6,377	($104,330)	(235,711)	($13,850)	$211,075	($45,059)	(130,076)
Interest Earnings from Loans	64,427	796,006	2,403,067	972,352	13,070	370,114	1,113,548	$404,662	6,137,246
Administration and Origination Fees	445,087				35,976				481,063
Other Income	61	1			112				174
Total Revenues	$18,357,635	$752,772	$2,409,444	$868,022	$5,686,152	$356,264	$1,324,623	$359,603	$30,114,515
EXPENDITURES:									
Program Administration/Set-Asides	$406,527	$4,566			$1,147,392	$31,004			$1,589,489
Total Expenditures	$406,527	$4,566			$1,147,392	$31,004			$1,589,489
Excess Revenues Over (Under) Expenditures	$17,951,108	$748,206	$2,409,444	$868,022	$4,538,760	$325,260	$1,324,623	$359,603	$28,525,026
OTHER FINANCING SOURCES:									
General Obligation Bond Proceeds	$2,665,000								$2,665,000
General Obligation Bond Premium			878						878
Operating Transfers In:									
Recycled Transfer from Drinking Water WRF		2,559,810							2,559,810
Recycled Transfer from Water Pollution Control SRF					42,893				42,893
Provide Recycled Funds for Program Transfer						2,559,810			2,559,810
Bonds Cost of Issuance	6,428	77,958			6,832				91,218
Administration and Origination Fees		162,293		282,250		35,976		22,842	503,361
Debt Service Sweep	566,962				432,862				999,824
Transfer Bond Anticipation Note to Debt Service	2,000,000								2,000,000
Transfer Bond and BAN Proceeds to Debt Service			1,600,000						1,600,000
Recycled Funds Transfers to Principal	533,622								533,622
Special Administration Transfer to Principal	1,000,000								1,000,000
Recycled Funds Transfers for Loans	1,777,135								1,777,135
Loan Loss Reserve Sweep	801,835				331,226				1,133,061
Total Other Financing Sources	$9,350,982	$2,800,061	$1,600,878	$282,250	$813,813	$2,595,786		$22,842	$17,466,612
OTHER FINANCING USES:									
Bond Principal			$550,000				$335,000		$885,000
Bond Interest			697,966				427,487		1,125,453
Bonds Cost of Issuance		71,471				(6,330)			65,141
Operating Transfers Out.									
Recycled Transfer to Water Pollution Control SRF						2,559,810			2,559,810
Recycled Transfer to Drinking Water WRF	42,893								42,893
Provide Recycled Funds for Program Transfer					2,559,810				2,559,810
Bonds Cost of Issuance	77,958	6,428				6,832			91,218
Debt Service Sweep			566,962				432,862		999,824
Administration and Origination Fees	444,543				35,976				480,519
Transfer Bond Anticipation Note to Debt Service			2,000,000						2,000,000
Transfer Bond and BAN Proceeds to Debt Service	1,600,000								1,600,000
Recycled Funds Transfers to Principal		533,622							533,622
Special Administration Transfer to Principal		1,000,000							1,000,000
Recycled Funds Transfers for Loans		1,777,135							1,777,135
Loan Loss Reserve Sweep				801,835				$331,226	1,133,061
Total Other Financing Uses	$2,165,394	$3,388,656	$3,814,928	$801,835	$2,595,786	$2,560,312	$1,195,349	$331,226	$16,853,486
Excess (deficiency) of revenues and other financing sources over (under) expenditures and other financing uses	$25,136,696	$159,611	$195,394	$348,437	$2,756,787	$360,734	$129,274	$51,219	$29,138,152
Fund Balance July 1, 2003	$104,945,145	$5,376,061	$1,447,039	$1,789,447	$54,404,183	$1,354,056	$944,352	$1,023,317	$171,283,600
Prior Year and Federal Revenue Adjustments	897	25,964	(879)		51,989	(48,819)			29,151
Fund Balance June 30, 2004	$130,082,738	$5,561,637	$1,641,554	$2,137,885	$57,212,958	$1,665,971	$1,073,625	$1,074,535	$200,450,903

[1] This schedule is prepared on a regulatory basis of presentation, rather than a GAAP [2] basis, as requested by the Environmental Protection Agency (EPA) for the Water Pollution Control and Drinking Water State Revolving Fund (SRF) Programs. This presentation separates certain regulated Revolving Fund (within the Fund) and Non-Revolving Fund (outside the Fund) activity by fund type. All proceeds from the EPA Capitalization Grant, corresponding state matching funds, and loan principal and interest repayments must be deposited into the Revolving Fund under Title VI of the Clean Water Act and Title XIV of the Safe Drinking Water Act. Other proceeds, including Administration and Origination Fees and Loan Loss Reserves are deposited into the Non-Revolving Fund and may be used for other water quality purposes under the federal acts mentioned above.

[2] Generally Accepted Accounting Principles (GAAP).

LEGISLATIVE AUDIT DIVISION

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James Gillett, Financial-Compliance Audit

INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the financial statements of the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs as of and for the fiscal year ended June 30, 2004, and have issued our report thereon dated January 24, 2005. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs' financial statements are free of material misstatement, we performed tests of their compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the departments' (Department of Environmental Quality and Department of Natural Resources and Conservation) internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

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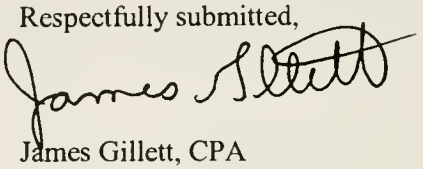
This report is intended solely for the information and use of the Legislative Audit Committee, the departments' management, the Montana State Legislature, and the federal Environmental Protection Agency and is not intended to be, and should not be, used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

Respectfully submitted,



James Gillett, CPA
Deputy Legislative Auditor

January 24, 2005